local communities; annexation plans of the municipalities in question; and any other relevant information.

(6) In states where rates or investment decisions are subject to approval by state regulatory authorities, there is reasonable expectation that such approvals will be forthcoming to enable repayment of the loan in full according to its terms.

(7) The experience and performance of the system's management is acceptable.

(8) In the case of joint ventures, the borrower has sufficient management control or other contractual safeguards with respect to the construction and operation of the jointly owned facility to ensure that the borrower's interests are protected and the credit risk is minimized.

(9) The borrower has implemented adequate financial and management controls and there are and have been no significant financial or other irregularities.

(10) The borrower's projected capitalization, measured by its equity as a percentage of total assets, is adequate to enable the borrower to meet its financial needs and to provide service consistent with the RE Act. Among the factors to be considered in reviewing the borrower's projected capitalization are the economic strength of the borrower's service territory, the inherent cost of providing service to the territory, the disparity in rates between the borrower and neighboring utilities, the intensity of competition faced by the borrower from neighboring utilities and other power sources, and the relative amount of new capital investment required to serve existing or new loads.

(c) RUS considers a loan to be feasible only if the borrower's electric system is year 2000 compliant, or if the borrower provides RUS with evidence, satisfactory to RUS, that it is taking measures necessary to ensure that its electric system will be year 2000 compliant on or before December 31, 1999. Year 2000 compliant means that product performance and function are not affected by dates before, during, and a reasonable time after the year 2000.

[57 FR 1053, Jan. 9, 1992; 57 FR 4513, Feb. 5, 1992, as amended at 60 FR 3731, Jan. 19, 1995; 63 FR 51793, Sept. 29, 1998]

§ 1710.113 Loan security.

(a) RUS makes loans only if, in the judgment of the Administrator, the security therefor is reasonably adequate and the loan will be repaid according to its terms within the time agreed.

(b) RUS generally requires that borrowers provide it with a first lien on all of the borrower's real and personal property, including intangible personal property and any property acquired after the date of the loan. This lien shall be in the form of a mortgage by the borrower to the Government or a deed of trust between the borrower and a trustee satisfactory to the Administrator, together with such security documents as RUS may deem necessary in a particular case.

(c)(1) When a borrower is unable by reason of preexisting encumbrances, or otherwise, to furnish a first mortgage lien on its entire system the Administrator may accept other forms of security, such as a pledge of revenues, if he or she determines such security is reasonably adequate and the form and nature thereof is otherwise acceptable.

(2) The Administrator, at his or her discretion, may approve the use of an indenture patterned after those indentures commonly used by utilities engaged in private market financing, in lieu of a mortgage as the security instrument for loans to power supply borrowers. The use of an indenture will be by mutual agreement of the borrower and the Administrator. The terms of each indenture and related loan agreement will be negotiated on a case by case basis to best meet the needs of the individual borrower and the Government. The provisions of the indenture and loan contract shall control, notwithstanding any provisions of 7 CFR Chapter XVII which may be in conflict therewith.

(d) In the case of loans that include the financing of electric facilities that are operated as an integral component of a non-RUS financed system (such as generation and transmission facilities

co-owned with other electric utilities), the borrower shall, in addition to the mortgage lien on all of the borrower's electric facilities, furnish adequate assurance, in the form of contractual or other security arrangements, that the system will be operated on an efficient and continuous basis. Satisfactory evidence must also be provided that the non-RUS financed system is financially sound and under capable management. Examples of such evidence include financial reports, annual reports, Security and Exchange Commission 10K reports if the system is required to file them, credit reports from Standard and Poor's, Moodys or other recognized sources, reports to state regulatory authorities and the Federal Energy Regulatory Commission, and evidence of a successful track record in related construction projects.

(e) Additional controls on the borrower's financial, investment and managerial activities appear in the loan contract and mortgage required by RUS.

[57 FR 1053, Jan. 9, 1992, as amended at 62 FR 7665, Feb. 20, 1997]

§ 1710.114 TIER, DSC, OTIER and ODSC requirements.

(a) *General.* Requirements for coverage ratios are set forth in the borrower's mortgage, loan contract, or other contractual agreements with RUS. The requirements set forth in this section apply to borrowers that receive a loan approved by RUS on or after February 10, 1992. Nothing in this section, however, shall reduce the coverage ratio requirements of a borrower that has contractually agreed with RUS to a higher requirement.

(b) *Coverage ratios.* (1) Distribution borrowers. The minimum coverage ratios required of distribution borrowers whether applied on an annual or average basis, are a TIER of 1.25, DSC of 1.25, OTIER of 1.1, and ODSC of 1.1. OTIER and ODSC shall apply to distribution borrowers that receive a loan approved on or after January 29, 1996.

(2) The minimum coverage ratios required of power supply borrowers, whether applied on an annual or average basis, are a TIER of 1.05 and DSC of 1.00.

(3) When new loan contracts are executed, the Administrator may, case by case, increase the coverage ratios of distribution and power supply borrowers above the levels cited in paragraphs (b)(1) and (b)(2), respectively, of this section if the Administrator determines that the higher ratios are required to ensure reasonable security for and/or the repayment of loans made or guaranteed by RUS. Also, the Administrator may, case by case, reduce said coverage ratios if the Administrator determines that the lower ratios are required to ensure reasonable security for and/or the repayment of loans made or guaranteed by RUS. Policies for coverage ratios following certain mergers, consolidations, and transfers of systems substantially in their entirety are in 7 CFR 1717.155.

(4) If a distribution borrower has in service or under construction a substantial amount of generation and associated transmission plant financed at a cost of capital substantially higher than the cost of funds under section 305 of the RE Act, then the Administrator may establish, in his or her sole discretion, blended levels for TIER, DSC, OTIER, and ODSC based on the respective shares of total utility plant represented by said generation and associated transmission plant and by distribution and other transmission plant.

(c) *Requirements for loan feasibility.* To be eligible for a loan, borrowers must demonstrate to RUS that they will, on a pro forma basis, earn the coverage ratios required by paragraph (b) of this section in each of the years included in the borrower's long-range financial forecast prepared in support of its loan application, as set forth in subpart G of this part.

(d) *Requirements for maintenance of coverage ratios*—(1) *Prospective requirement.* Borrowers must design and implement rates for utility service to provide sufficient revenue (along with other revenue available to the borrower in the case of TIER and DSC) to pay all fixed and variable expenses, to provide and maintain reasonable working capital and to maintain on an annual basis the coverage ratios required by paragraph (b) of this section. Rates must be designed and implemented to produce at least enough revenue to